No. 406

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CHARLES ELMORE CROPLEY
CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1949

and No. 179 Miscellaneous

INDEPENDENCE LEAD MINES COMPANY,
AN ARIZONA CORPORATION,
Petitioner,

—against—

ALMA R. KINGSBURY AND OLGA MARQUARDT,
Respondents,

Ex Parte INDEPENDENCE LEAD MINES COMPANY,
AN ARIZONA CORPORATION,
Petitioner,

MOTION FOR LEAVE TO FILE PETITION FOR A WRIT OF CERTIORARI AND PETITION FOR A WRIT OF CERTIORARI

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INDEX

	PAGE
Motion for Leave to File Petition for a Writ of Certiorari	1
Petition for a Writ of Certiorari and Brief in Support Thereof	3
Summary Statement of Matter Involved	4
Opinions Below	4
Principal Questions Passed on by the Court of Appeals for the Ninth Circuit	4
Summary of Facts	6
Basis of Court's Jurisdiction	14
Questions Presented	15
Reasons Relied on for Allowance of Writ	17
Prayer	23
Brief in Support of Petition for Writ of Certiorari	25
Reported Opinions	25
Specification of Errors	25, 26

PAGE

ARGUMENT ---------- 28

Statutes Involved ---------- 28

POINT I

Two judges, of a seven-judge court, cannot deny a petition for rehearing *en banc* addressed to the whole court. This court has heretofore established that a minority of judges does not constitute a full court. Surely two judges cannot assume to act with finality where a court is composed of seven judges--- 29

POINT II

An alleged officer and director of a corporation cannot fraudulently connive with two large stockholders and give them dividends out of trust property held for distribution to other stockholders; and the corporate management, consisting of one alleged officer and director, cannot through his wrongful control violate a trust to all the corporation stockholders by giving two large stockholders all of a dividend to the exclusion of the other stockholders ------ 30

POINT III

Even though an alleged acting president of a corporation had been discharging his duties under color of authority, and with some general acquiescence of the stockholders, he is neither a *de jure* nor *de facto* officer, in respect to stockholders or third parties who knew in fact that he was not an officer of the corporation, in any character, either *de jure* or otherwise. The Court of Appeals held that such an officer as described above was at least a *de facto* officer (tr. pp. 133, 134) -------- 36

PAGE

POINT IV

Fraud is not in issue in litigation so as to be concluded by a stipulated judgment between the parties, giving two large stockholders all of the company's remaining trust stock, where an alleged officer and director of a corporation connives and colludes with two large stockholders who knew that the corporation officer had robbed and was robbing the corporation of its trust stock, before such stipulated judgment was entered ---------- 40

POINT V

There is collusion and connivance between parties entering into a stipulated judgment, where one part is under duress from the other party through an implied threat of a disagreeable alternative to him in his fiduciary capacity, if he does not act in violation of his duty ---------- 44

POINT VI

A stipulated judgment entered into by an alleged officer of a corporation who was also its attorney, and two large stockholders of the corporation, should be set aside where the officer of the corporation corruptly sold out the corporation's interest ---------- 47

CONCLUSION ---------- 49

PAGE

APPENDIX

Opinion and Dissent of Court of Appeals Dated February 28, 1949 (Ninth Circuit) ---------- i

Opinion and Dissent of Court of Appeals Dated August 8, 1949 (Ninth Circuit) ---------- xxiv

Amended Order of Court of Appeals Dated August 22, 1949 (Ninth Circuit) ---------- xxviii

Amended Dissent of Chief Judge Denman Dated August 23, 1949 (Ninth Circuit) ---------- xxix

PAGE

TABLE OF CASES CITED

Carpenter v. Clark, 217 Mich. 63, 185 N. W. 868, 870 ---------- 39

Cutting v. Woodward, 255 F. 633, 634, Ninth Circuit ---------- 36

Geddes v. Anaconda Copper Mining Co., 254 U. S. 590, 599, 41 S. Ct. 209, 65 L. Ed. 425 ------ 36

Groveland Improvement Company v. Farmers' Supply Company, 25 Wash. 344-346, 65 Pac 529 38

Harr v. Pioneer Mechanical Corporation, 65 F. 2d. 332-334, 2nd Circuit ---------- 31

Heimbaugh v. Hitchcock, 115 Kansas 182, 222 Pac. 114 ---------- 34

Independence Lead Mines Company, an Arizona Corporation, v. Alma R. Kingsbury and Olga Marquardt, 175 Fed. 2d., page 983 ---------- 4, 25

Johnson v. Moore, 31 Arizona 137, 145, 250 Pac. 995 ---------- 34

Morse v. Metropolitan S. S. Co., 87 N. J. Eq. 217, 100 Atl. 219, 221, 222 ---------- 34

National Lock Company v. Hogland, 101 F. 2d. 576, 582, 7th Circuit ---------- 31

PAGE

Ryan v. Old Veteran Mining Company; 37 Idaho 625 at page 636, 218 Pac. 381, at page 384 ------ 35

Textile Mills Corporation v. Commissioner of Internal Revenue, 314 U. S. 326-333 ---------- 29

U. S. v. Johnston, 316 U. S. 649, 650 ---------- 29

United States v. Throckmorton, 98 U. S. 61, 25 L. Ed. 93, page 95 ---------- 48

PAGE

STATUTES CITED

28 U. S. C. A., 1651 (a) ---------- 1, 14, 15, 28

28 U. S. C. A., 1254 (1) ---------- 1, 14, 15, 28

TEXTS CITED

Cyclopedia, Federal Procedure, Vol. 8, page 386-- 31

Fletcher Cyclopedia Corporations, Perm. Ed. Vol. 2, Sec. 384, page 163 ---------- 37

Fletcher Cyclopedia Corporations, Perm. Ed. Vol. 2, Sec. 385, page 163 ---------- 38

Fletcher Cyclopedia Corporations, Permanent Edition, Vol. 13, Sec. 5810 ---------- 33, 34

Fletcher Cyclopedia Corporations, Permanent Edition, Vol. 13, Sec. 5811, at page 127 -------- 32

Fletcher Cyclopedia Corporations, Permanent Edition, Sec. 5785, Vol. 13 ---------- 34

Restatement of the Law of Judgments, Sec. 122, comment 'a' page 593, comment 'b' page 594 -- 47

Restatement of the Law of Judgments, page 597 -- 45

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—against—

ALMA R. KINGSBURY AND OLGA MARQUARDT,
Respondents,

Ex Parte INDEPENDENCE LEAD MINES COMPANY,
AN ARIZONA CORPORATION,
Petitioner.

MOTION FOR LEAVE TO FILE PETITION FOR A WRIT OF CERTIORARI

To the Honorable Chief Justice of the United States and the Associate Justices of the Supreme Court of the United States:

Petitioner herein, Independence Lead Mines Company, an Arizona Corporation, and a resident of the State of Arizona, moves the Court for leave to file the petition hereto annexed for a Writ of Certiorari pursuant to Section 1651 (a) of the Judicial Code (28 U. S. C. A., 1651 (a)), and Section 1254, Subsection (1) of the Judicial Code (28 U. S. C. A., 1254 (1)) to review the judgment entered in this case on February

28, 1949 (tr. p. 151), and further moves the Court to grant judgment in accordance with the petitioner's prayer and to grant such other relief as may be just in the premises.

Dated October 18, 1949.

INDEPENDENCE LEAD MINES COMPANY,
AN ARIZONA CORPORATION,

Petitioner.

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Petitioner.

PETITION FOR A WRIT OF CERTIORARI AND BRIEF IN SUPPORT THEREOF

Petition

Independence Lead Mines Company prays for the issuance of a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit directing a reversal of that certain order and judgment entered by the said Court on February 28, 1949, which affirmed the judgment of the District Court in said cause, and likewise directing the nullification of that certain order entered by said Court of Appeals on August 8, 1949, and amended by said Court on August 22, 1949, denying the petition of petitioner in said Court for rehearing *en banc.*

Summary Statement of Matter Involved
Opinion Below

The District Court did not write an opinion. The opinion of the Court of Appeals for the Ninth Circuit with dissenting opinions is reported in 175 Fed. 2d., Page 983 *et seq.* (See Appendix pp. i to xxx.)

Principal Questions Passed on by the Court of Appeals for the Ninth Circuit

(1) The Court of Appeals determined (two judges in a panel of three judges of a seven-judge court), by the opinion of two judges (the Chief Judge dissenting), that it was empowered to deny a petition *en banc* addressed by the petitioner to the whole court of seven judges (tr. p. 152 *et seq.*).

(2) The Court of Appeals (panel of three judges, the Chief Judge dissenting) held that respondents, the largest stockholders in the petitioner corporation, could retain stock received by them from the corporation, and which comprised a large share of a dividend previously declared to other stockholders, even though the petition seeking to reopen a stipulated judgment between petitioner and respondents, giving to respondent stockholders such stocks, alleged that such judgment was entered by and through the collusion and connivance of the respondents with the president of said petitioner corporation, who they knew, before entry of the stipulated judgment, was not an officer of the petitioner corporation, either *de jure* or *de facto*,

and who the respondents knew, prior to the entry of the stipulated judgment sought to be reopened, had robbed the corporation of over two hundred thousand shares of trust stock, and who had informed the respondents of such fact prior to the stipulated settlement entered into between the president of said corporation and the respondent stockholders. (Note—Allegations of petition to reopen were admitted by respondent's motion to dismiss, tr. p. 79, no answer filed.)

(3) The Court of Appeals decided that no fraud was pleaded in an action to set aside a judgment, entered on behalf of petitioner corporation by its president and attorney, where the petition to set aside such judgment alleged, that the petitioner company's attorney corruptly sold out his client's interest and fraudulently colluded and connived with the adverse party (respondents) to do so, which facts were known and participated in prior to said judgment by the adverse parties, respondents here.

(4) The Court of Appeals determined that no fraud was practiced because of the failure of respondents and counsel to advise the District Court, at the time of the entry of the stipulated judgment between petitioner and respondents, that respondents were receiving from such stipulatd judgment all of the trust stock of the petitioner previously declared as a dividend to other stockholders, and the Court of Appeals also determined that no fraud was practiced even though the District Court was not advised by respondents who

knew, that the president and attorney for said petitioner company entering into the stipulation on behalf of petitioner, had robbed the company of some two hundred thousand shares of the trust stock and was entering into such stipulation for the purpose of preventing exposure.

Summary of Facts

The petitioner, through its alleged president and attorney, entered into a stipulated judgment with the respondents in the District Court of Idaho on June 22, 1946, and judgment and decree was entered pursuant thereto on June 24, 1946 (tr. pp. 45-50, inclusive). The stipulation and judgment entered pursuant thereto arose out of an action of respondents against petitioner in the lower court wherein respondents claimed that they were entitled to share in a stock dividend previously declared by petitioner to other stockholders of Clayton Silver Mines stock (tr. pp. 7, 8, 9). The complaint of respondents set forth that petitioner company's originally authorized stock was divided into 4,000,000 shares of a par value of $1.00 per share and that such stock was divided into two kinds of stock, there being 3,000,000 shares designated as "common" stock and 1,000,000 shares designated as "preferred" stock; that the preferred stock was non-assessable and had certain preferences otherwise. Complaint stated that on February 10, 1932, the stockholders, by resolution duly adopted at a stockholders' meeting, amended the Articles of Incorpora-

tion of the petitioner and eliminated the preferred stock, authorizing in lieu of said stock 1,000,000 shares of so-called common stock Class A and providing that such stock should be non-assessable; that the petitioner corporation for value received issued to the Mines Finance Corporation, an Idaho corporation, upon the amendment, the 1,000,000 shares of common stock Class A, and that on the 31st day of December, 1941, the Mines Finance Corporation assigned and transferred 666,667 shares of the common stock Class A to respondents, Alma R. Kingsbury, and 333,333 shares to one Herman Marquardt, now deceased, husband of respondent, Olga Marquardt; that thereafter the petitioner corporation issued 666,667 shares of said common stock Class A to Alma R. Kingsbury, and after probate of the said estate of Herman Marquardt, Olga Marquardt, respondent, received 333,333 shares of the common stock Class A. The respondents in their original action set out that the petitioner, Independence Lead Mines Company authorized the distribution on September 1, 1944, of most of the Clayton stock (750,000 shares, tr. p. 67) to the shareholders of the Independence Lead Mines Company on the basis of one share of Clayton to each four shares of the Independence Lead Mines stock owned by stockholders; that the Independence Lead Mines Company, petitioner here, refused to distribute any of the Clayton stock to the respondents who claimed that their common stock Class A was entitled to enjoy all of the rights and benefits of the other common stock of the Independence Lead

Mines Company (tr. p. 4, 5, 6, 7, 8). Petitioner, Independence Lead Mines Company, filed motion to dismiss in the District Court on July 25, 1945, and the same was denied on November 30, 1945 (tr. p. 34, 35), and petitioner filed its answer on April 29, 1946, in which answer the petitioner denied that 1,000,000 shares of common stock Class A were ever lawfully issued. Petitioner further denied that there was any consideration of any nature whatsoever for any of the transfers alleged by respondents to them of the common stock Class A. The petitioner corporation in its answer contended that the transfers of the common stock Class A to the respondents constituted a fraud on the corporation (tr. p. 38, 39, 40, 41, 42). Respondents amended their complaint and filed said amended complaint on May 22, 1946 (tr. p. 43, 44, 45). They asked that in the event the petitioner was unable to deliver the proper ratio of stock that it be compelled to make the plaintiffs whole by payment to them of stocks and cash. On the 22nd day of June, 1946, petitioner and respondents, through counsel, entered into a stipulation (tr. p. 45, 46, 47), which stipulation was incorporated in a judgment and decree entered the 24th day of June, 1946 (tr. p. 48, 49, 50), whereby respondents were to surrender 400,000 shares of the common stock Class A of the appellant corporation and were to have and to receive in return 170,000 shares of the Clayton Silver Mines stock and $10,050.00 in cash. The judgment also decreed that respondent, Alma R. Kingsbury, was the bona fide owner of 400,000 shares

of the common stock Class A of the petitioner corporation, and that respondent, Olga Marquardt, was the bona fide owner of 200,000 shares of the common stock Class A of the petitioner, Independence Lead Mines Company, and that all of said stock has, possesses and is entitled to the same identical rights, privileges and benefits as the common stock of the petitioner, Independence Lead Mines Company. The order decreed that the only difference between the common stock and the common stock Class A was that the latter was not subject to assessment (tr. p. 49, 50).

On June 23, 1947, *petitioner corporation, Independence Lead Mines Company, filed its motion to vacate and set aside that judgment* (*tr. p.* 50-64, *inclusive*), hereafter referred to as the petition, *and on December* 11, 1947, *filed its amendment to motion to vacate and set aside judgment* and reopen said cause to allow Independence Lead Mines Company to file a proper answer and to reopen said cause for trial, which will hereafter be referred to as the amended petition (see amendment to petition of petitioner tr. p. 65-76, incl.)

The amended petition set forth that at the time of the amendment of the petitioner Independence Lead Mines Company's Articles of Incorporation to create the common stock Class A designation, representations were made by the Independence Lead Mines Company's president and secretary to all of its stockholders, that said stock would be held in the treasury of

the company and would only be exchanged for the purchase of other mining properties; that no mining properties were purchased pursuant to the representations made to the stockholders; that Henry B. Kingsbury and Herman Marquardt in about the year 1923 were the president and secretary of the Independence Lead Mines, Ltd., the predecessor in interest to the petitioner, Independence Lead Mines Company, and that they formed the Mines Finance Corporation, of which Henry B. Kingsbury became president and Herman Marquardt became secretary and of which company they were the sole stockholders (tr. p. 51, 52, 53). The amended petition alleged that the purpose of the Mines Finance Corporation was to take and receive the funds of the Independence Lead Mines, Ltd., which were secured by the levying of assessments on the common stock of the latter company; that the Mines Finance Corporation had no source of revenue or income. The amended petition set forth that thirteen assessments were levied upon the petitioner company for the benefit of the Mines Finance Corporation and Henry B. Kingsbury and Herman Marquardt; that during or shortly after the year 1930 the said Kingsbury and Marquardt controlled absolutely the petitioner corporation here and the Mines Finance Corporation and that they secured to themselves the 1,000,000 shares of common stock Class A of the petitioner, Independence Lead Mines Company, fraudulently and without any consideration; that by reason of the deaths of Henry B. Kingsbury and Herman

Marquardt, the present respondents, who are the widows of said deceased persons, came into the possession and alleged ownership of the 1,000,000 shares of common stock Class A of the Independence Lead Mines Company; that Henry B. Kingsbury and Herman Marquardt had defrauded the company and all of its stockholders by making no distinction in the certificates of the Independence Lead Mines Company of the classes of the stock, and that they had, by keeping permanent control of the petitioner corporation, caused the fraudulent issue of the common stock Class A to be made (tr. p. 54, 55, 56, 57, 58). The amended petition alleged that since the death of Herman Marquardt in August of 1942, the petitioner corporation had been controlled and dominated by one F. C. Keane of Wallace, Idaho, who acted as president without any right or authority, as he had not been a stockholder since some time in the year 1940, and that the said Keane had appointed two other directors who likewise had no right or authority to act as such; that this Board of Directors in August of 1944 had caused a resolution to be passed providing for the payment of Clayton Stock as dividends to the holders of Independence Lead Mines Company stock, on a one-to-four ratio, and specifically declaring in the resolution that the Class A common stock should not participate because of a question as to its validity (tr. p. 66, 67, 68); that said F. C. Keane, who was in complete control of the petitioner corporation, had sold and disposed of almost all of the assets of the company for his own use and bene-

fits, as had been set forth in a complaint for receivership (tr. p. 82), which complaint also alleged that said Keane had misappropriated the property of the petitioner corporation and had withheld information required by the regulations of the Securities and Exchange Commission for a number of years while he was engaging in his misappropriations. The amended petition also alleged that the respondents have been for some time by far the largest stockholders of the petitioner corporation and that they lived in the Town of Wallace, Idaho, where said company maintained its principal office, and that they also maintained and operated the largest brokerage business in Wallace, known as Pennaluna and Company, and that they knew of the affairs of the petitioner corporation and that they knew that the company had no legal Board of Directors and that they knew that F. C. Keane was applying the proceeds of the sale of Independence Lead Mines Company assets to his own use and was dissipating the same. It was also alleged that the respondents were such large stockholders of the petitioner corporation that they were in virtual control and that they would not interfere with the said F. C. Keane because they knew they could get a good settlement in the cause of action instituted by them if they did not do so; that in July of 1945 *before respondents instituted action in the lower Court they and their attorney, in writing notified the Clayton Silver Mines, Inc., to stop any further transfers of Clayton Stock belonging to Independence Lead Mines Company, and*

that the respondents threatened an injunction action, and that they knew about the dissipation of the petitioner's funds prior to bringing their action in the District Court against the petitioner, and did nothing about it (tr. p. 71, 72). The amended petition also alleged that knowledge of the misappropriation by the said F. C. Keane of the funds of the Independence Lead Mines Company was known by the respondents prior to any settlement and that the said F. C. Keane had sent one John Sekulic, an emissary of his, to the respondents to propose to them a settlement and to show them, the respondents, that they had better take a settlement of all of the remaining stock of the Clayton Silver Mines, Inc., owned by the Independence Lead Mines Company, to-wit, 170,000 shares; that the said emissary Sekulic was paid $10,000.00 to arrange this settlement, and that after said negotiations between Keane, Sekulic and the appellees, the stipulated judgment heretofore referred to was enterd (tr. p. 73, 74, 75, 76). The amended petition alleged that Sekulic informed respondents that they had better accept his offer or take nothing, and that respondents were fully advised as to Keane's activities but settled with him even though the validity of their common stock Class A was in dispute.

Motion to dismiss was filed by the respondents on the 15th day of December, 1947 (tr. p. 79). Orders of dismissal were entered, pursuant to argument, by the District Court (tr. p. 79, 80, 81, 82).

On appeal, following this action, to the United States Court of Appeals for the Ninth Circuit, the order of the District Court was affirmed by that Court on February 28, 1949. (Majority opinion of two judges of a three-judge panel tr. p. 128-140, incl.). The Chief Judge of said Court wrote a dissenting opinion (tr. p. 140, 150, incl.).

On August 8, 1949, the Court of Appeals for the Ninth Circuit (two judges of a three-judge panel) denied respondents' petition for rehearing *en banc* and the Chief Judge of said Court sitting on the panel dissented (tr. p. 152). On August 22, 1949, two judges of the Court of Appeals for the Ninth Circuit entered an order amending the previous order denying petition for rehearing *en banc,* the amended order reading as follows: "The petition for rehearing is denied" (tr. p. 152). The Chief Judge of said Court of Appeals who sat on the three-judge panel dissented again to such amendment on August 23, 1949 (tr. p. 153 *et seq.*).

Basis of Court's Jurisdiction

The jurisdiction of this court is invoked pursuant to Section 1651 (a) of the Judicial Code, (28 U. S. C. A. 1651 (a)), which provides that the Supreme Court and all congressional courts may issue all Writs necessary or appropriate in aid of their respective jurisdictions and agreeable to the usages and principles of law, and section 1254 (1) of the Judicial Code, (28 U. S.

C. A. 1254 (1)), which provides that cases in the Court of Appeals may be reviewed by Writ of Certiorari granted upon the petition of any party to any civil or criminal cases, before or after rendition of judgment or decree.

Questions Presented

The principal questions involved are:

(A) Whether this case is appropriate for the exercise of the Court's power to issue all necessary Writs in accordance with 28 U. S. C. A. 1651 (a), and whether this case may be reviewed by Writ of Certiorari upon the petition of petitioner corporation for such review of the judgment of the Court of Appeals, Ninth Circuit, in the Civil Case below upon which the judgment of said Court of Appeals has been rendered? (28 U. S. C. A. 1254 (1)).

(B) Whether two judges in a panel of three judges of the Court of Appeals for the Ninth Circuit, which is comprised of seven judges, can deny a petition *en banc* addressed to the whole court of seven judges; and whether those two judges alone can assume to act for the seven judges of the court to which a petition for rehearing is addressed?

(C) Whether the two largest stockholders in a corporation can collude and connive fraudulently with the president and attorney of the corporation to de-

prive the other stockholders in the corporation of their right to receive trust stock of the corporation, held by the corporation for distribution to such stockholders, by a stipulated judgment conveying all of such trust stock to the two large stockholders who without notice to the other interested stockholders, but with knowledge of fraud and theft by the president and attorney of the company, of large blocks of trust stock, accept such trust stock in the stipulated judgment?

(D) Whether there is fraud in a stipulated judgment, sufficient to set the same aside upon application of the defrauded corporation party, where the president and attorney of the defrauded corporation party, corruptly sold out its interest and fraudulently colluded and connived with two large stockholders, who were adverse parties, and knew all of the facts of such corruption before the entry of such stipulated judgment against the defrauded corporation party?

(E) Whether there is fraud in a stipulated judgment sufficient to set the same aside upon application, where the president and counsel of the defrauded corporation party, joined with the adverse parties and their attorney, in the entry of the judgment against the defrauded corporation party, and where neither the president and counsel of the defrauded corporation nor the adverse stockholders parties, or their counsel, disclosed to the District Judge signing the stipulated judgment, that such judgment would de-

prive the defrauded corporation party of all of its trust stock previously declared as a dividend to other stockholders?

(F) Whether fraud was present in a stipulated judgment between a corporation party and two large stockholders of said corporation, who were adverse parties, where the president and counsel of the corporation party, and the adverse stockholder parties entered into a stipulation and judgment against the corporation party, with knowledge by the adverse parties, that the said president and attorney for the corporation party had robbed the corporation party of over two hundred thousand shares of trust stock, prior to the time of the entry into the stipulation by the party corporation and the adverse parties?

(G) Whether an alleged officer and director of a corporation can fraudulently connive and, through such fraudulent connivance, bind a corporation party to a stipulated judgment entered into, with two large stockholders of the corporation, where those two stockholders knew, that the president and director of said corporation was not an officer or director of such corporation *de jure* or *de facto,* prior to the entry into said stipulated judgment?

Reasons Relied on for Allowance of Writ

(A) The Courts of Appeals of the various circuits which are a part of the Federal Judicial system are

usually the Courts of last resort in the run of ordinary cases arising from litigation in the Federal Courts of original jurisdiction. The question of whether or not two judges of a Court of Appeals, comprised of seven judges, can determine with finality, litigation and questions directed to the entire Court, poses an outstanding and highly important question of public importance to all litigants in the Federal Courts.

If two judges of a seven-judge court can act with finality in that court, then such fact should be clearly made known to all litigants in the Federal Courts, who then can proceed with a complete understanding, that a full complement of judges in a circuit is unnecessary to a final determination of litigation. It will then be known, that upon the entry of judgment by a minority panel of such court, the litigant is foreclosed from further proceedings in such court, and that he may proceed by appropriate means to seek review in the Supreme Court of the United States. However, it would appear that no sound reason exists for the existence of a specified number of judges comprising a Court of Appeals, if, in fact, a minority panel can itself deprive all of the other judges of the court from passing on a question addressed to the whole court. Likewise, it would appear, that indecision will be created in the minds of litigants in respect to either the advisability, or necessity, of further proceedings to a final unqualified judgment; and it further appears that if a small minority of judges of a court can de-

clare the law in respect to litigants addressing an issue to the full court, then the work of this court will be greatly increased. In view of the fact that the Courts of Appeals are in most instances the courts of last resort for most litigants, a question of great importance is presented, both in respect to whether or not the obligation of the Appellate Court is met in respect to its litigants, and whether or not this Court should exercise power of supervision to determine conclusively the question of the finality in the Courts of Appeals, of the order and judgment of a minority of such court.

(B) Stockholders of corporations are in many instances out of touch with the intricate operation of the corporation through the policy making decisions of its board of directors and high officers. Corporate organization, as we know it, is such that in many instances hundreds and thousands of stockholders are scattered throughout the entire United States and its possessions, in many different occupations and pursuits. Many of these people depend upon their holdings and dividends for security in their later years. These stockholders likewise depend, as they have a right to do, upon the honesty of the officials in charge of the corporations in which they hold stock. Those officials are, in most cases, far removed from the stockholders and in many instances are unknown to the stockholders except by name. Likewise, the activities of the corporation, directed through its offi-

cers and directors, are usually not known to the widely scattered little stockholders except from the reports made by the corporation to the stockholders. Thus, by the very nature of corporate organization, there is established a fiduciary relationship to the stockholders, and the highest degree of trust relationship should exist on behalf of the directors and officers of a corporation, with its stockholders. If two large stockholders of a corporation can connive fraudulently with the alleged president, director, and attorney of the corporation, and thereby secure through a fraudulently stipulated judgment unbeknown to the other stockholders, a large amount of trust stock, held as a dividend for small stockholders of the corporation, then there is a complete breakdown of the ethical duty to stockholders of the officers of the corporation, and there is a complete departure from the trust and fiduciary relationship that should be mandatory in any dealings of the directors and officers of a corporation which effect the large body of its small stockholders.

(C) It is of great public importance to determine also, whether an alleged president, director, and attorney of a corporation, known by two large stockholders to be neither a *de jure* or *de facto* officer, can connive fraudulently with those two large stockholders of the corporation to enter a stipulated judgment against the corporation to the exclusion of rights of the large number of small stockholders. It is believed

that this Writ should be allowed because it conclusively appears that an alleged officer and attorney of a corporation, who was neither the president or a director *de jure* or *de facto,* and who acted as one of counsel for the corporation, corruptly sold out the interest of the corporation and its small stockholders by a stipulated judgment with two large stockholders, who knew of the corruption of the alleged officer and attorney for the corporation, but who took the benefits of such judgment despite foreknowledge of the character and criminal activities of the alleged officer and attorney of the corporation.

(D) The law should not sanction the validity of a stipulated judgment between a corporation and two large stockholders, entered into by the corporation through an alleged officer, and its attorney, who joined with the adverse parties and their attorney, in presenting a judgment to a Federal District Court, without advising the court that the judgment would deprive the corporation of all of its trust stock, previously declared as a dividend to other stockholders. This Writ, we believe, should be allowed so that such a procedure in the entry of a fraudulent judgment between an alleged corporation officer seeking to cover up his defalcations by compromise, and two large stockholders who prior to the stipulated judgment knew of the defalcations, can be nullified and so that the corporation can be allowed to prove its charges

and recover the trust stock which it held for the small stockholders.

(E) In this case there has been wrongful control by an alleged corporate officer, who has violated a trust for all the small stockholders, by depriving them of their share of a distribution of corporate assets which had been declared to them as dividends. This alleged officer fraudulently connived with two large stockholders, and entered into a stipulated judgment between the two large stockholders and the alleged president, which deprived the corporation of all of the assets of the corporation, which were to be distributed to the other stockholders.

(F) Likewise, the Court of Appeals below, has decided an important question of local law, which is probably in conflict with the local decisions applicable. The court below has decided that this suit is not maintainable, even though the action of the corporation in seeking to set aside a stipulated judgment, shows a fraudulent and a wrongful dealing with the corporate assets, by the alleged president, director, and attorney of the corporation with two large stockholders. This holding of the court is probably in conflict with the law of Arizona, the State of incorpora-

tion of the petitioner, and with the law of Idaho, the State in which this litigation began (see pages 34, 35, 36 *infra*).

(G) This Court, it is respectfully suggested, should allow this Writ for the further reason that the court below has in effect, decided that counsel for petitioner, acting fraudulently against the petitioner, and in connivance with two large stockholders, respondents here, can stipulate a judgment with those two stockholders, who had foreknowledge of the counsel's fraud; when this court has held that a judgment cannot stand, where the facts show, that a party's counsel has corruptly sold out his client's interest (see pages 47, 48 *infra*).

Prayer

For the reasons hereinabove set forth and discussed in detail with supporting authorities in the accompanying brief, your petitioner prays for a Writ of Certiorari to the Court of Appeals for the Ninth Circuit, or such other Writ as to the Court may seem just and appropriate, to be issued out of this Court and directed to the Court of Appeals for the Ninth Circuit, to the end that the judgment of the Court of Appeals for the Ninth Circuit may be reviewed by

this Honorable Court and relief granted by this Honorable Court in the premises.

October 18, 1949.

INDEPENDENCE LEAD MINES COMPANY,
AN ARIZONA CORPORATION,
Petitioner,

BY: R. MAX ETTER

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1949

No.----------Miscellaneous

INDEPENDENCE LEAD MINES COMPANY,
AN ARIZONA CORPORATION,
Petitioner,

—against—

ALMA R. KINGSBURY AND OLGA MARQUARDT,
Respondents,

Ex Parte INDEPENDENCE LEAD MINES COMPANY,
AN ARIZONA CORPORATION,
Petitioner.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

Reported Opinions

The District Court below did not write an opinion. The opinion of the Circuit Court of Appeals and dissenting opinions is reported in 75 Fed. 2d., pp. 983-993.

There are also set out in the appendix the opinions and orders of the court in respect to the proceedings (see appendix pp. i to xxx).

Specification of Errors

It is contended that the Court of Appeals below erred in the following respects, to-wit:

(A) The Court erred when two judges of the Court, in a panel of three judges, denied a petition for rehearing *en banc* which was addressed to the whole Court of Appeals composed of seven judges.

(B) The Court erred in affirming the District Court's order, which granted respondents motion to dismiss, by holding that respondents, two largest stockholders in petitioner corporation, could connive fraudulently with the president and attorney of the corporation to deprive the other stockholders in the corporation of their right to receive trust stock of the corporation, held by the corporation for distribution to such other stockholders, by a stipulated judgment conveying all of such trust stock to the two large stockholders, without notice to the interested stockholders, and when the large stockholders with knowledge of fraud and theft by the president and attorney of the company, of large blocks of trust stock, took such other trust stock by the stipulated judgment.

(C) The Court erred in holding that there was not fraud in a stipulated judgment, sufficient to set the same aside upon the application of the defrauded corporation party, where the president and attorney of the defrauded corporation party, corruptly sold out its interest, and fraudulently colluded and connived with two large stockholders, who were adverse parties, and knew all of the facts of such corruption before the

entry of such stipulated judgment against the defrauded corporation party.

(D) The court erred in holding that there was not fraud in a stipulated judgment sufficient to set the same aside, where the president and counsel of the defrauded corporation party joined with the adverse parties and their attorney in the entry of the judgment against the defrauded corporation party, and where neither the president and counsel of the defrauded corporation party or the adverse stockholder parties, or their counsel, disclosed to the District Judge signing the stipulated judgment, that such judgment would deprive the defrauded corporation party, of all of its trust stock previously declared as a dividend to other stockholders.

(E) The Court erred in holding that there was not fraud present in a stipulated judgment between a corporation party and two large stockholders of said corporation who were adverse parties, sufficient to set such judgment aside, where the president and counsel of a corporation party and the adverse stockholder parties entered into a stipulation and judgment against the corporation party, with knowledge by the adverse parties, that the said president and attorney for the corporation party had robbed the corporation party of over two hundred thousand shares of trust stock, prior to the time of the entry into the stipulation by the party corporation and the adverse parties.

(F) The Court erred in holding that an alleged officer and director of a corporation could bind the corporation to a stipulated judgment, with the two largest stockholders of the corporation, when those two stockholders knew prior to the entry by them into the stipulated judgment, that the so-called officer and director of the corporation was not an officer or director of the corporation, *de jure* or *de facto.*

ARGUMENT
Statutes Involved

The statutes bearing on the jurisdiction of this Court to issue the Writ are Section 1651 (a) of the Judicial Code (28 U. S. C. A., 1651 (a)), and Section 1254, Subsection (1) of the Judicial Code (28 U. S. C. A., 1254 (1)).

28 *U. S. C. A.,* 1651 (a) "The Supreme Court and all courts established by Act of Congress may issue all writs necessary or appropriate in aid of their respective jurisdiction and agreeable to the usages and principles of law . . ."

28 *U. S. C. A.,* 1254 "Cases in the Courts of Appeals may be reviewed by the Supreme Court by the following methods:

(1) By Writ of Certiorari granted upon the petition of any party to any civil or criminal case, before or after rendition of judgment or decree . . ."

POINT I

Two judges, of a seven-judge court, cannot deny a petition for rehearing en banc addressed to the whole court. This court has heretofore established that a minority of judges does not constitute a full court. Surely two judges cannot assume to act with finality where a court is composed of seven judges.

The cases cited below justify the statement made:

> *Textile Mills Corporation vs. Commissioner of Internal Revenue,* 314 U. S. 326-333, *et seq.; U. S. vs. Johnston,* 316 U. S. 649, 650.

In *Textile Mills Corporation v. Commissioner,* the Court states at page 333:

> "We cannot conclude, however, that the word 'court' as used in those other provisions of the Judicial Code means only three judges. That would not only produce a most awkward situation; it would on all matters disenfranchise some circuit judges against the clear intendment of 118. Nor can we conclude that the word 'court' means only three judges when the court is sitting, but all the judges when other functions are performed. Certainly there is no specific authority for that construction. And it is difficult to reach that conclusion by inference. For to do so would be to imply that Congress prohibited some circuit judges from participation in the most important function of the 'court' (the hearing and the decision of appeals), though allowing all of them to perform the other functions. Such a prohibition as respects the ordinary responsibilities of a judicial office should be inferred only under compelling necessity, since a court usually will consist of all the judges appointed to it. That necessity is not present here. The ambiguity in the

statute is doubtless the product of inadvertence. Though the problem of construction is beset with difficulties, the conclusion that 117 provides merely *the permissible complement* of judges for a circuit court of appeals results in greater harmony in the statutory scheme than if the language of 117 is taken too literally."

The above is a clear pronouncement of what constitutes the "Court" and is a clear determination of the right of a litigant to consideration by the whole court. We respectfully urge that neither the opinion, nor order of a minority panel for the Ninth Circuit denying petition for rehearing *en banc* in this case, is the opinion or order of the whole Court.

POINT II

An alleged officer and director of a corporation cannot fraudulently connive with two large stockholders and give them dividends out of trust property held for distribution to other stockholders; and the corporate management, consisting of one alleged officer and director, cannot through his wrongful control violate a trust to all the corporation stockholders by giving two large stockholders all of a dividend to the exclusion of the other stockholders.

Petitioner here is an Arizona corporation and is qualified and authorized to transact business in the State of Idaho (tr. pp. 2, 10, 28, 33). The law of the State of Arizona is controlling in respect to the rights of stockholders against corporate officers who fraudulently connive with other stockholders, here with two large stockholders, to give them dividends through a fraudulent stipulated judgment against the corporation.

National Lock Company vs. Hogland, 101 F. 2d. 576, 582, 7th Circuit;

Harr vs. Pioneer Mechanical Corporation, 65 F. 2d. 332-334, 2nd Circuit.

The amended petition, the facts of which were admitted by respondents' motion to dismiss, alleges participation by the respondents in the fraud of the corporate respondents' officer, in the procurement of the stipulated judgment (tr. pp. 50-64, incl.; tr. pp. 65-76, incl.). The petition is a narration of complete fraud and it would be a hypertechnical problem to attempt to segregate fraud of so-called intrinsic character from the extrinsic. An applicable approach here is set out in *Cyclopedia, Federal Procedure,* Vol. 8, Page 386 *et seq.*:

> "Any wilful misrepresentation inducing the court to render an improper and unjust decree or to include improper provisions may be made the basis of such an application, as where the court is induced by misrepresentations of fact to sign the particular decree.
>
> One of the most troublesome distinctions in the law, almost as celebrated as that between 'latent' and 'patent' ambiguities in applying the parol evidence rule, is that between 'extrinsic' and 'intrinsic' fraud as ground for equitable relief from a judgment. That understanding of jurisprudence, which the legal profession at least should have, would have been furthered by discarding such expressions long ago; but they seem to have some unfortunate and perpetuating allure.

> Sometimes it has been sought to fasten the distinction upon the difference between fraud upon the court and other fraud; but this requires at least a broad view of what constitutes fraud 'upon the court' as the conduct or deceit which commonly forms the basis for relief is directed at the opposite party, deceiving him, rather than the court. *Probably no universally satisfactory test can be laid down.*" (Emphasis supplied.)

None of the transactions, by which respondents secured the common stock Class A, or transactions prior thereto, concerning such stock, engaged in between predecessors in interest of the respondents and the petitioner corporation were known to the petitioner corporation's new board of directors until about the 26th day of May, 1947 (tr. pp. 62-75-76). The situation here is not one where minority stockholders have dealt with petitioner corporation, nor does it concern a majority stockholder dealing with petitioner corporation at arms length. The situation here presented shows a course of dealing between petitioner corporation through its alleged president and director and two large stockholders, respondents, where the respondents had not only actual knowledge of the corporation affairs, but exercised an actual domination of the corporation (tr. pp. 71-72-73-74-75). In *Fletcher Cyclopedia Corporations,* Permanent Edition, Vol. 13, Section 5811 at Page 127, we find:

> "A stockholder, even though he owns a majority of the stock, does not occupy a trust relation towards the other stockholders merely because of

his holding of such stock, and it has been vigorously asserted that majority stockholders are in no case trustees for the minority. But while, in a narrow and restricted sense, it cannot be said that the holder or holders of the majority of the stock occupy a relation of trust, yet it can be said, in a larger and broader sense, that they sustain a fiduciary relation to the holders of the minority stock and the corporation. *And according to most of the decisions, a trust or fiduciary relation arises under certain circumstances. The actual control of the property 'is the basis in all of the cases of the trust relation.'* Thus it is held that when a number of stockholders combine to constitute themselves a majority in order to control the corporation as they see fit, *they become for all practical purposes the corporation itself,* and assume the trust relation occupied by the corporation towards its stockholders. It has been held that if a majority stockholder actually dominates the company, although not himself an officer, through his control of a majority of the board of directors, he stands in the same fiduciary relation to the other stockholders as he would sustain if he were a director or other officer. Of course, if a majority stockholder is also a director and the president or other chief officer of the corporation, he is a trustee." (Emphasis supplied.)

Majority stockholders are obliged to act in good faith as far as the rights of the minority stockholders are concerned.

"Majority stockholders, to the extent to which they control the corporation, must act in good faith, as far as the rights of minority stockholders are concerned. Their transactions must be free from fraud, and must not amount to a wanton destruction of the rights of the minority. It is a

breach of duty to manipulate the business of the company in their own interests to the injury of minority stockholders. However, there is no duty on the part of majority stockholders to assist the corporation financially in its money difficulties and thereby shield it from financial destruction."

Fletcher Cyclopedia Corporations, Permanent Edition, Vol. 13, Sec. 5810;

Morse vs. Metropolitan S. S. Co., 87 N. J. Eq. 217, 100 Atl. 219, 221, 222.

Likewise, a majority of stockholders cannot help themselves to all of the corporate assets to the absolute exclusion of minority stockholders. See Sec. 5785, *Fletcher Cyclopedia Corporations,* Permanent Edition, Vol. 13, which says:

"Majority stockholders have no power to distribute or divide corporate assets among themselves, to the exclusion of minority stockholders. If they do so, minority stockholders may, in a proper case, obtain relief by a suit in equity. However, owners of all the stock may dedicate the corporate property to their private use, where there are no creditors or third persons who may object."

Heimbaugh vs. Hitchcock, 115 Kansas 182, 222 Pac. 114.

In the case of *Johnson v. Moore,* 31 Arizona 137, 145, 250 Pac. 995, there was a connivance by corporate officers, where the corporate officers declared a dividend of the proceeds from the sale of certain company assets, which they paid over to some stockhold-

ers to the exclusion of other stockholders. The latter brought suit against the corporation and the stockholders who received the dividend monies. The Supreme Court of Arizona held, 31 Ariz. at page 145, 250 P. at page 998:

> "* * * If the officers of defendant corporation had merely retained in their custody as such officers plaintiff's share of the proceeds of the sale, his remedy would indeed be *ex contractu,* but the allegation of the complaint is that the corporation and the individual defendants, with the 'knowledge, consent, aid, and connivance one with the other,' divided among the defendants, not only their pro rata of the $42,000 but also that which should have been paid plaintiff. If the trustee of a sum of money pays it to a person not entitled to receive it, with full knowledge on the part of the latter as to the facts, and his active participation in the illegal payment, it is undoubtedly a breach of trust, for which both the trustee and the recipient of the money are liable as in conversion. *White v. Sherman,* 168 Ill. 589, 48 N. E. 128, 61 Am. St. Rep. 132; *Duckett v. National Mechanics' Bank,* 86 Md. 400, 38 A. 983, 39 L. R. A. 84, 63 Am. St. Rep. 513; *American Trust & Banking Co. v. Boone,* 102 Ga. 202, 29 S. E. 182, 40 L. R. A. 250, 66 Am. St. Rep. 167; 38 C. J. 2055. * * *"

A suit by the stockholders is maintainable in this situation and the Idaho Courts and Federal Courts likewise have so held. In *Ryan v. Old Veteran Mining Company;* 37 Idaho 625 at page 636, 218 Pac. 381, at page 384, the Court said:

> "Directors of corporations act in a fiduciary capacity. They hold the corporate property in

trust, and any attempt on their part to divert the use of such property to their personal profit or interest is a violation of the trust imposed by virtue of the office. *Riley v. Callahan Mining Co., supra.* (28 Idaho 525, 155 P. 665.)"

Likewise see:

Geddes v. Anaconda Copper Mining Co., 254 U. S. 590, 599, 41 S. Ct. 209, 65 L. Ed. 425;

Cutting v. Woodward 255 F. 633, 634, 9 Circuit.

POINT III

Even though an alleged acting president of a corporation had been discharging his duties under color of authority, and with some general acquiescence of the stockholders, he is neither a de jure nor de facto officer, in respect to stockholders or third parties who knew in fact that he was not an officer of the corporation, in any character, either de jure or otherwise. The Court of Appeals held that such an officer as described above was at least a de facto officer (tr. pp. 133, 134).

Considering the majority opinion's statement, but confining it, as it respected Keane's relationship to many of the stockholders, it does not follow that respondents here who dealt with Keane, *knowing in fact that he was not even an officer de jure of the petitioner corporation,* are free from liability to petitioner corporation and its common stockholders for the Clayton Silver Mines Company stock and money, which they received from the corporation, as a result of a collusive, fraudulent, stipulated judgment.

The reason for the *de facto* doctrine has been stated as follows:

> "The reason for the rule was also well stated by Justice Clopton in Alabama as follows: 'The doctrine of the validity of the acts of officers *de facto* rests on public policy and justice. The official dealings of directors *de facto* with third persons are sustained as rightful and valid, on the ground of continuous acquiescence by the corporation, and suffering them to hold themselves out as having such authority; *thereby inducing others to deal with them in such capacity.* The theory of the doctrine of officers *de facto,* and the principles sustaining the validity of their official acts, are that, though wrongfully in office, yet exercising power and functions appertaining to such office, *justice and necessity require, for the protection and preservation of the rights and interests of third persons,* that their acts, within the scope of official authority and duty, shall be sustained.' " (Italics supplied.) (*Fletcher Cyclopedia Corporations,* Perm. Ed., Vol. 2, Sec. 384, page 163.)

It seems clear from the above that if the stockholders of a corporation, or the corporation by acquiescence, allows officers to act and to deal with third persons, then the official dealings of those officers *de facto,* are binding and valid—*if, however, such conduct of the corporation, in its acquiescence, thereby induces others to deal with them in that capacity. That situation is not present here.* The petition to vacate the judgment alleges as facts admitted by respondents' motion to dismiss, that neither F. C. Keane nor two other so-called directors were in fact lawful directors

of the petitioner corporation (tr. page 58); and the petition further alleges that respondents well knew these facts and well knew that there was no legal board of directors—*the respondents in fact knew that neither F. C. Keane nor the others* were officers (tr. pages 61, 70, 71, 85). There was no question of respondents being misled by Keane, the petitioner, or petitioner's stockholders, and there is no question involved concerning the protection of their rights, if any, as innocent third parties.

The rule applicable to respondents is as follows:

> "*Exception where person dealing with officers not misled.* The *de facto* rule will not be extended to a case where a person dealing with alleged corporate officers is not misled, nor induced to believe that he is dealing with legal officers, but has knowledge that the person pretending to be an officer is not a *de jure* officer." (*Fletcher Cyclopedia Corporations,* Perm. Ed., Vol. 2, Sec. 385, page 163.)

A Washington case cited to the text, namely, *Groveland Improvement Company vs. Farmers' Supply Company,* 25 Wash. 344-346, 65 Pac. 529, states in part as follows:

> "The rule that third persons dealing with *de facto* officers of a corporation are protected in such dealings has no application. *The rule is designed for the protection of innocent third persons, who have dealt with such officers without knowledge of their true character.* But here the evidence offered tended to show that the manager

of the respondent, who represented it in the making of the lease, was one of the persons intruding into the offices of the corporation which purported to execute the lease; and, as he had knowledge of the lack of authority of the intruders to represent the corporation, his knowledge must be imputed to the respondent." (Italics supplied.)

Also, it has been stated as follows:

"(4) But different considerations arise when the protection of third parties is not involved. A person clothed with apparent authority may be a *de facto* officer to the general public and to innocent third persons, but not such where his own rights are involved, *nor to those fully advised of his status,* nor as against one showing a *prima facie* right to an office he unlawfully withholds." (Italics supplied.)

(*Carpenter vs. Clark,* 217 Mich. 63, 185 N. W. 868, 870.) (Italics supplied.)

The discussion and authority cited above determines that respondents did not acquire any right, in the capacity of innocent parties, that would clothe them with immunity from the present action of the petitioner corporation, by reason of any dealings with *de facto* officers. Surely this petitioner corporation has a right to prove, if it can, that the respondents dealt with individuals, particularly the president, whom respondents knew had no legal right, or any right at all, to represent the petitioner corporation.

POINT IV

Fraud is not in issue in litigation so as to be concluded by a stipulated judgment between the parties, giving two large stockholders all of the company's remaining trust stock, where an alleged officer and director of a corporation connives and colludes with two large stockholders who knew that the corporation officer had robbed and was robbing the corporation of its trust stock, before such stipulated judgment was entered.

The record in this cause, and particularly the undisputed allegations of fact in the petitioner's petition to reopen and vacate the judgment, indicate, in our opinion, that there never was a litigation of any issue between petitioner and respondents, which in law or equity could sustain the then president of the petitioner, F. C. Keane, in generously handing over to the respondents every last single share of Clayton stock, held in the treasury of the petitioner, and including all of the trust stock, held for the benefit of common stockholders, by reason of a dividend previously declared to them. It must be conceded, that it was quite a considerable time after respondents commenced an action to compel the payment to them of dividend Clayton stock by the petitioner (tr. page 2, *et seq.*), that petitioner's president, F. C. Keane, who was then acting illegally as president of the petitioner corporation, filed any answer in the cause (tr. pages 38-43, incl.). It appears that Keane, who was then acting as president of the petitioner corporation, made no answer of any kind going to the merits of respondents' complaint until *almost one whole year had expired*

from the date of filing the complaint. Within two months after Keane, illegally acting as president of the corporation, filed an answer in the cause, respondents amended their complaint (tr. page 43), entered into a stipulation with Keane and petitioner corporation (tr. page 45), and entered a stipulated judgment against the petitioner (tr. page 48).

Within one month after respondents commenced their action in June of 1945, *they caused notice in writing to be sent to the Clayton Silver Mines Company and its officers at its office in Wallace, Idaho, to stop forthwith all further transfers of Clayton stock belonging to the Independence Lead Mines Company; and respondents threatened that if said Clayton Silver Mines Company did not comply with said notice, they, the respondents, would immediately bring injunction proceedings to prevent any further disposition or transfer of such stock* (tr. pages 72, 73). This notice was obviously sent to Clayton Silver Mines Company because of respondents knowledge of Keane's personal wrongful appropriations, and because after sale by Keane, transfers were being made of the trust stock to the new holders. The record indicates that there were no further sales of Clayton Silver Mines stock by F. C. Keane for the personal account of F. C. Keane, who was acting as president, or at all, *after the year* 1945 (tr. pages 97, 98, 99, 100). We think it obvious that respondents' notice to Clayton Silver Mines Company was definitely effective; that the Clayton

Silver Mines Company did heed the notice; and that Keane was likewise informed or had knowledge of said notice and threat; because it does not appear that Keane made any further sales or transfers after the notice given in July of 1945 even though the petitioner company still had in its treasury, at the time of respondents' notice and threat of injunction, the sum of approximately 170,000 *Clayton shares.* (In connection with the above, see Note 5, majority opinion, tr. pp. 137, 138 and reference tr. pp. 146, 147, Note 7, dissenting opinion.)

The record further discloses that all of these remaining 170,000 shares were retained by Keane, until they were awarded to respondents here by stipulated judgment of respondents and the then acting president, Keane. Keane at the time of respondents' notice and threat of injunction directed toward Clayton Silver Mines, had misappropriated 218,000 shares of Clayton Silver Mines Company stock, held and owned by petitioner corporation, and it does not appear that after respondents' notice and threat a single share was further disposed of. Respondents got the balance. (In this connection, likewise see table and breakdown of Clayton stock held by Independence, in dissenting opinion in Court of Appeals tr. pp. 149, 150).

Keeping the above facts in mind, we turn to the petitioner's petition to vacate the judgment, entered on behalf of respondents with Keane the defalcating al-

leged president of petitioner. Such petition has already been the subject of much discussion in the opinions of the court of appeals. However, it is most important to point out, that in analyzing the sequence of events related above and keeping them in mind at all times along with the implications logically deducible from them, we find that the petition alleges that *respondents knew all about Keane's misappropriations* and dissipation of the company assets; that they knew the stipulated judgment entered into between them and Keane, purportedly representing the petitioner, would give them stock of other common stockholders already impressed with a trust character; and that they were definitely told by one John Sekulic, an emissary of the defalcating alleged president Keane, of all the facts and circumstances of the petitioner corporation's situation and Keane's defalcations, before they took the Clayton stock by the collusive judgment (tr. pages 73, 74, *et seq.*)

It therefore appears upon the undisputed facts in the petition, the truth of which are admitted by respondents' motion to dismiss directed against petitioner's petition to reopen and vacate, that the fraud was never in issue and was never litigated or concluded by the judgment in favor of the respondents. It would appear rather, that the *fraud and collusion determined the judgment,* and actively and positively prevented any proper real contest of any issues between the respondents and petitioner. Therefore, inasmuch as the

petition to reopen directly alleges by facts pleaded, the participation of the respondents with the petitioner in the fraud, the respondents, by reason of such participation, prevented any real contest or litigation on the merits of the controversy existing between respondents and petitioner.

POINT V

There is collusion and connivance between parties entering into a stipulated judgment, where one party is under duress from the other party through an implied threat of a disagreeable alternative to him in his fiduciary capacity, if he does not act in violation of his duty.

The Court of Appeals in speaking of collusion and duress, indicated that such collusion must have been practiced or connived at by the successful party, and that it must be such as prevented the losing party from fully and fairly presenting his case or defense (tr. pp. 138, 139). Ordinarily it is conceded, that fraud which was at issue or which could have been dealt with in litigation concluded by a judgment, cannot be made the basis of an attack on the judgment. However, the facts in the case in issue, indicate that the rule is inapplicable here. In the present instance, the fraud which *should have been made an issue* (tr. pages 39-41, inc.), could not be, and was not dealt with in the proceedings leading up to the collusive judgment, because the collusion between the president of the petitioner corporation and respondents, *prevented its litigation.* The effect, of course, *was that the fraud was not litigated.*

Likewise, the latter part of the court's reference (tr. p. 139) to comment "e" is somewhat incomplete. The latter part of the comment (see page 597, *Restatement of the Law of Judgments*) is as follows:

> "*Duress has the same effect as collusion and is similar to it.* It differs from collusion only in that there is a threat of a disagreeable alternative to the fiduciary if he does not act in violation of duty to the beneficiary instead of a benefit conferred upon or promised to him for such action." (Italics supplied.)

In view of the above, and keeping in mind the allegations, undenied, of 'connivance,' we suggest that duress and collusion were present, and are properly pleaded by petitioner in the petition to vacate; that such acts, charged as having been employed by respondents, are admitted by respondents' motion to dismiss. It must be remembered that respondents by stipulated judgment settled with petitioner corporation, through Keane, and received from it, through Keane, all of its shares of Clayton Silver Mines Company stock, besides a sizeable amount of cash, in June of the year 1946 (tr. pages 48, 49, 50), although prior to that time respondents knew by reason of the visit from Mr. Keane's emissary, John Sekulic (tr. pages 73, 74, 75) that Keane had misappropriated and taken unto himself 218,000 shares of Clayton Silver Mines Company stock, belonging to the petitioner corporation and its stockholders including respondents. Despite the knowledge of the misappropriations of Keane, which were

brought to the attention of the respondents prior to the stipulated judgment entered into with them by the petitioner through Keane, *they did nothing but take all of the balance of the Clayton Silver Mines Company stock remaining in the corporation treasury; they did not expose Keane; they did not investigate Keane; they did not call for a stockholders meeting; they did not try to remove Keane; they did not report their knowledge to any officer of the law or State's attorney; they did not take any step against Keane that would be consistent with the usual, ordinary action which would be taken by any stockholder against an officer of his corporation who such stockholder knew to be corrupt, and who such stockholder knew had misappropriated practically all of the assets of the corporation for his own benefit. Surely with this in mind, the only possible logical deduction to assume therefrom is that respondents made no complaint or report of any kind, nor took any action of any kind, because of the payment to them in the stipulated judgment by Keane, of the balance of all Clayton Silver Mines Company stock remaining in petitioner corporation's treasury.* Duress of Keane seems apparent, for the facts indicate that after the settlement was made, no action of any kind was taken by these respondents, despite their knowledge of Keane's deeds, *and it remained for the Securities and Exchange Commission to compel the disclosure of Keane's misdeeds to the other stockholders* (tr. pp. 75, 76, 89, 90). No disclosure whatsoever was made or attempted by respondents,

who had knowledge of the misdeeds, and who profited in the settlement. Likewise, pertinent rules and important observations are made, in respect to the above situation, in the following: *Restatement of the Law of Judgments*—Section 122, comment 'a', page 593; comment 'b', page 594, the latter part thereof which is as follows:

> "Likewise a person who has been harmed by a judgment obtained as the result of collusion between his representative and the representative of the other party is entitled to equitable relief upon discovery of the facts if other methods of relief are not then available."

Paragraph 'c' and illustrations, page 595; and paragraph 'd', page 596.

POINT VI

A stipulated judgment entered into by an alleged officer of a corporation who was also its attorney, and two large stockholders of the corporation, should be set aside where the officer of the corporation corruptly sold out the corporation's interest.

In this case there was no contest of any kind, and there is no merit in the contention that the collusive judgment is *res adjudicata* in regard to respondents.

> "Where the unsuccessful party has been prevented from exhibiting fully his case, by fraud or deception practiced on him by his opponent, as by keeping him away from court, a false promise of a compromise; or where the defendant never had knowledge of the suit, being kept in ignor-

ance by the acts of the plaintiff; *or where an attorney fraudulently or without authority assumes to represent a party and connives at his defeat; or where the attorney regularly employed corruptly sells out his Client's interest to the other side*— these, and similar cases which show that there has never been a real contest in the trial or hearing of the case, are reasons for which a new suit may be sustained to set aside and annul the former judgment or decree, and open the case for a new and fair hearing." *United States vs. Throckmorton,* 98 U. S. 61, 25 L. Ed. 93, page 95. (Emphasis supplied.)

In this case the respondents knew that Keane, the officer, director and attorney of the company was giving to them all of the trust stock of the corporation, and they likewise knew of the condition of the corporation as a result of the thefts from it by Keane. Nevertheless they actively participated, as the first and only recipients of all of the petitioner corporations remaining trust stock, through a stipulated judgment (tr. pp. 72, 73, 74; dissent Chief Judge Denman tr. pp. 154, 156).

CONCLUSION

1. The amended petition contains direct and undenied allegations of connivance and fraud, practiced by respondents and their predecessors, and the petition alleges an active participation and connivance in a fraudulent judgment secured by the respondents for their own exclusive benefit. There is present, fraud, and a suppression and exclusion of the equitable rights of the petitioner and its assessable stockholders.

2. There is nothing before the court to justify any assumption that the compromise settlement was favorable to the petitioner, or was as favorable to the petitioner, as it was to the respondents. (Dissent, Chief Judge Denman tr. p. 156).

3. The allegations of the petition eliminate any consideration of respondents' argument that they dealt with any *de jure* or *de facto* directors of petitioner corporation. It is in fact affirmatively alleged in the amended petition, that the plaintiffs knew that F. C. Keane and the officers of the company were not legal officers, and could not act in accordance with law on behalf of the corporation in any dealings with respondents. True, the directors could have been *de facto* directors in dealings with other persons or stockholders, if those other persons or stockholders had no knowledge that Keane and the directors were not legal directors. That situation is not present here.

4. The president of petitioner corporation, F. C. Keane, acted illegally and dissipated practically all of the corporate assets. His actions were in disregard of the rights of assessable stockholders, who have for many years paid assessments on their stock through good times and bad, to keep the petitioner corporation in business. F. C. Keane acted illegally as petitioner corporation's president, and while so acting, he sought to protect and save himself by resort to a collusive stipulated judgment and fraudulent compromise.

5. Respondents here dealt with Keane as a director and an officer of the corporation, knowing full well that he was legally incapable of acting in such capacity, and they dealt with him directly and through his emissary Sekulic, as the attorney for the petitioner corporation, with knowledge of his activities as set forth above. They were knowingly parties to a collusive stipulated judgment and fraudulent compromise, and they actively participated and connived with Keane in his dual capacity as the attorney for the petitioner corporation protecting Keane, and as Keane the defalcating officer. The respondents have actively lent aid and sustenance to Keane, and have deliberately and with knowledge of the facts, helped themselves to the remaining assets of the trust stock of the petitioner corporation. Respondents well knew, that by so doing, they were depriving all other stockholders of any participation in the stock dividend of the petitioner declared to them.

It appears also that respondents are getting more than they expected when they commenced their original action. The judgment of the District Court in favor of the respondents provides that, in addition to awarding them all of the trust stock, the respondents shall have judicial approval in respect to common class A non-assessable stock which they held. The judgment of the Court provides:

> "That the common stock "Class A" of the defendant, Independence Lead Mines Company, including 600,000 shares owned by the plaintiffs, as aforesaid, *has, possesses, and is entitled to the same and identical rights, privileges and benefits, share for share, as the common stock of the said Independence Lead Mines Company, the only difference or distinction between the common stock and the common stock 'Class A' being that the latter is not subject to assessment.*" (Italics supplied.) (Tr. page 49, 50.)

From the above, it can be seen that the important controversy, which is of the greatest importance to the petitioner corporation and to all of its assessable common stockholders, has gone by default of Keane and respondents, and as a result of their collusion and connivance in securing judicial approval.

It is indeed ironic that the decree mentions *"the only difference or distinction between common stock and the common stock Class 'A' being that the latter is not subject to assessment."* In other words, the district court order says that common stock Class "A" is

entitled to profits and dividends and all advantages of a financial nature accruing to any of the common stock held by common stockholders in many states of the United States; and the appeals court has further judicially approved a situation, where the common stockholders who have paid assessments on their stock to keep the corporation in business, must continue to do so when assessments are levied; and the court is likewise judicially approving respondents' right to be free from any contribution, assessment, or payment to the corporation for any expense necessary to the corporation's life. At the present time respondents are given a lifetime moratorium on the payment of any stock obligation for the upkeep and life of this corporation. We submit to this Honorable Court that this situation has fraudulently been brought into existence, without even allowing the corporation to defend against the unjust claims of respondents, because of the connivance and collusion, between respondents and Keane, the alleged president of the petitioner corporation.

Furthermore, if the judgment of the court is to stand, we will be confronted with a situation in which the respondents may claim and possibly now sustain their *right to vote* their 600,000 shares of Class "A" common stock, something which they have never been able to do before they secured the stipulated judgment. The appeal court's opinion constitutes judicial approval, of the transfer of tremendous control to re-

spondents, without even allowing the corporation stockholders a voice to oppose the same. The right to vote stock is most valuable, and the control of the respondents by virtue of the validity of their 600,000 shares of common stock, Class "A," will be exercised in perpetual derogation of the right of the corporation to ever question its validity.

Respectfully submitted,

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APPENDIX

Opinion and Dissent of Court of Appeals Dated February 28, 1949

In the United States Court of Appeals for the Ninth Circuit

INDEPENDENCE LEAD MINES COMPANY, a corporation,
Appellant,

vs.

ALMA R. KINGSBURY AND OLGA MARQUARDT,
Appellees.

No. 11,959

Feb. 28, 1949

Upon Appeal from the District Court of the United States for the District of Idaho, Northern Division

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BEFORE: DENMAN, HEALY, and ORR, Circuit Judges

HEALY, Circuit Judge

This is an appeal from an order dismissing a petition of appellant, hereafter called Independence, to vacate a judgment. The background of the litigation may be summarized as follows:

Originally the authorized capital stock of Independence consisted of three million shares of common assessable stock and one million shares of preferred.

None of the preferred was outstanding. In 1932 the articles were amended by eliminating the authorized preferred stock and creating in lieu thereof one million shares of nonassessable Class A common. Upon the amendment the Class A common was issued to Mines Finance, a corporation wholly owned by two men, Kingsbury and Marquardt, who were respectively president and secretary of Independence. Kingsbury died at an unspecified date. In 1941 Mines Finance assigned two-thirds of the Class A common to Kingsbury's widow and one-third to Marquardt, and Independence issued to those individuals certificates evidencing the shares. In 1942 Marquardt died and his shares were distributed to his widow who thereupon obtained a formal transfer of the stock to herself. Thus on the books of Independence the two widows, who are appellees here, appeared as holders of all the Class A common.

Independence owned [redacted]d in its treasury 1,001,000 shares of the stock of Clayton Silver Mines Company. The common stockholders were insistent upon the distribution of the Clayton stock, or the bulk of it, as a dividend. Accordingly the directors of Independence, in August of 1944, adopted a resolution providing that 750,000 of the Clayton shares be distributed to the common stockholders on the basis of one share of Clayton to four shares of Independence. The resolution provided that the Class A common was not to

participate in the distribution "for the reason that there is a question as to the validity" of that stock.

Independence commenced actively to distribute the Clayton stock and by June 1946 all but 73,175 shares of the dividend declared had been distributed.[1] Appellees in June of 1945 filed suit against Independence in the court below alleging their ownership of the Class A common, their right to participate in the dividend equally with other stockholders, and the refusal of Independence to recognize their right. They asked that Independence be ordered to distribute to them 250,000 shares of the Clayton stock together with a sum alleged to have been paid to Independence as a dividend thereon. Independence moved to dismiss and its motion was denied in November of 1945. Later, no answer having been filed by Independence and extensions of time given it to answer having expired, appellees moved for a default. Thereupon Independence answered.

The answer denied that the Class A common had been lawfully issued for value received or for any other consideration. It alleged that at the time of the transfer of the stock to Mrs. Kingsbury and to Marquardt the latter was the alter ego of Independence and that the transfer was made without knowledge of its other officers; and further, that at the time of the transfer

[1]The resolution required that the stockholders send in their certificates in order that the receipt of the distribution might be evidenced by a stamp thereon. Some Independence shares appear for a long while to have been traded in ex-dividend on the exchange.

of the Marquardt stock to his widow the officers of Independence were not aware of the true facts. Finally, the answer denied that the Class A common was issued or outstanding and alleged that if so it was void and of no effect.

Subsequent to the joinder of issue in the suit the parties entered into a stipulation for the entry of judgment to the effect that the claim of the appellees to 250,000 shares of the Clayton stock be rejected and that they have from Independence 170,000 shares thereof, and no more; that appellees surrender to Independence 400,000 shares of their Class A common; that it be adjudged that they are the bona fide owners of the balance, namely 600,000 shares, with rights identical to those of the common stock; and finally that Independence pay to the appellees the sum of $10,050. Judgment to this effect was entered by the court on June 29, 1946.[2]

The petition for the vacation of this judgment was filed in 1947 after the election by Independence of a new board of directors. Two of its main paragraphs were extensively amended after a motion to dismiss it had been interposed. Appellees' motion was then renewed, and Independence having declined to plead further the court dismissed the amended petition as insufficient. This appeal followed.

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[2]It appears that throughout the suit Independence was represented by several attorneys.

The defenses of want of consideration, invalidity and fraud in the original issuance to Mines Finance of the Class A common, as set up in the answer, are repeated in the petition with much evidentiary detail and in great amplified form. The substance of the defenses, however, is concededly identical in the two pleadings. Since fraud in this respect was in issue in the litigation concluded by the judgment it can not be made the basis of an attack on the judgment. Donovan v. Miller, 12 Idaho 600; United States v. Throckmorton, 98 U. S. 61, 68; Toledo Scale Co. v. Computing Scale Co., 261 U. S. 399; 49 Corpus Juris Secundum, Judgments, pp. 738-740. Independence concedes that such is the general rule, but argues in its brief that the principle is not applicable here for the reason that appellees at all times had knowledge of the invalidity of their holdings. Such knowledge, however, is not pleaded, and we need not inquire what might be its effect if it had been pleaded. There is no averment in the petition that appellees knew that fraud had been practiced by their predecessors in the acquisition of the stock; and no facts are set out which would in good conscience preclude them from resorting to the courts for an adjudication of their disputed claim.

The balance and bulk of the petition is devoted to an attempt to show fraud in the procurement of the judgment. On this phase Independence argues that collusion between its president on the one side and appellees on the other prevented it from making its

defense. What the court has to determine is whether the contention finds adequate support in the facts alleged in the petition.[3]

The petition avers that since the death of Marquardt in 1942 Independence had been under the control and domination of one Keane, its acting president; that Keane was currently disqualified to act as an officer because no longer a stockholder; and that the two other directors serving with and appointed by Keane were not stockholders, hence were also disqualified from acting. No stockholders meeting, it is said, had been held for eight years. It is averred that appellees, well knowing these facts, dealt with Keane in the settlement of their suit. From the recitals of the petition as a whole, however, it is plain that Keane and the other directors were at least de facto officers. Cf. Fletcher, Cyc. Corp., Vol. 2, Ch. 11, §§372-390. Keane was and for years had been in open and unchallenged possession of the office, discharging its duties under color of authority and with the acquiescence of the generality of stockholders. The latter appear to have recognized his authority to act for the corporation; and there is no allegation that they themselves were unaware of the true nature or infirmities of his tenure. The very dividend from which this litigation stemmed had been declared and was in process of distribution

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[3]The Idaho rule, like the rule generally, is that in a proceeding of this nature the facts constituting the fraud must be definitely and positively alleged, Zounich v. Anderson, 35 Idaho 792.

by Keane and his associates acting as officers and directors. The common stockholders had sought the dividend at their hands, recognized their authority to declare it, and claimed and accepted its fruits. We think Independence, speaking here ostensibly for the common stockholders, is in no position to challenge Keane's official status.

Again, it is alleged that Keane was currently engaged in the sale of large blocks of the Clayton stock held by Independence and was corruptly dissipating the proceeds or applying them to his own use. Appellees are alleged on information and brief to have had knowledge of Keane's plundering of the corporation and that they took no steps to oust him for the reason that they could obtain a better settlement of their own claims "by dealing with the so-called president who desired to conceal the true condition of the affairs of the said Company and his own misdeeds in connection with its operations." It is alleged that appellees "claimed to be" such large stockholders of Independence that "they were in virtual control thereof," yet took no action to curb Keane's mismanagement. On this phase it is to be noted that there is no allegation that appellees owned or claimed to own any stock in Independence other than the Class A common, their title to which was being currently denied and contested by Independence. The court is not informed of the means by which, in the circumstances, they could act effectively. Indeed, if the petition be

taken at its face value they had in law n[o]w no standing as stockholders or right to interfere in the [the] corporate affairs. In any event we think they were [a]re not obliged to halt their suit until the internal affairs o[f]s of the corporation were corrected.

The petition, in substance, alleges furt[h]urther that prior to the settlement of the suit Keane had s[o]d sold 218,000 of the Clayton shares belonging to Indepen[d]endence and had appropriated the proceeds to his own [a]n account; that 613,000 Clayton shares had been distri[b]tributed as dividends to the common stockholders of I[n] Independence[4]; and that there was thus left in the treas[u]easury a balance of 170,000 Clayton shares. It is alleged t[h]d that as the result of a conference between Keane and[d] one Sekulic the latter approached appellees with th[e] the proposition that Keane would, in settlement of their [a]ir demands, turn over to them all the Clayton shares rem[a]remaining in the treasury, to-wit 170,000 shares, plus the [s]the sum of $10,050 in cash, they, however, to relinquish[q]uish to Independence 400,000 shares of their Class A co[m]common, retaining the balance as their own; and that Sek[u]Sekulic informed appellees that if they would not accept[e]ept the proposal they would receive no dividend in conse[q]nsequence of any judgment secured against Independence [f]ce for the reason that Keane would sell and dispose of t[h]f the remaining

[4]It appears in the petition that 2,744,700 shares onl[y] only of the ordinary common stock of Independence had been issued. Thus Thus, on the basis of one share of Clayton to four of Independence, it requi[r]equired 686,175 shares of Clayton to fill the dividend requirements as restricte[d]tricted to the ordinary common stock. Clayton shares to the number of 73,175 h[a]175 had not been called for by common stockholders. The balance of 613,000[0] 3,000 shares had been distributed.

Clayton stock and apply the funds to his own use. It is averred that appellees accepted the proposal with knowledge that they would thereby secure all the remaining Clayton stock, including 73,175 shares "being held in trust" by Independence for the benefit of the common stockholders who had not yet received their dividend.

The foregoing paragraph is a summary of a series of allegations running through eight pages of the printed record. Independence argues that against this background the settlement reflects, not a reasoned compromise of a doubtful lawsuit, but merely the panicky surrender of all available assets by an officer under pressure or threat of exposure.

In urging this view counsel for Independence ask us to heed Dryden's couplet: "Errors, like straws, upon the surface flow; he who would search for pearls must dive below." We have done so and come up, among other things, with a small pearl or two possibly worth mentioning. Made a part of the petition is an audit of the affairs of Independence prepared by a certified public accountant, covering the year 1945 and the three prior years, and forming part of a report submitted by Keane as president of Independence to the Securities and Exchange Commission in March 1947. The audit fully discloses Keane's sales of Clayton shares referred to in the petition, and also shows that he was currently acquiring substantial amount of Clayton

stock on behalf of Independence. It would appear from the submission of this audit and report that within nine months after the entry of the judgment Keane himself made a public disclosure of the internal affairs of Independence and of his own irregularities as its president. One is accordingly obliged to take a dim view of the argument, here so heavily stressed, that Keane's anxiety to avoid exposure of those matters was the moving factor inducing the settlement.

On other considerations, too, this central thesis of the petitioner hardly survives analysis. It is obvious that Keane's misdeeds were irrelevant to the issues joined in the suit and would not be disclosed in the ordinary course of a trial of those issues. If Independence was really in position to establish fraud in the acquisition by Kingsbury and Marquardt of its Class A common it would have been greatly to Keane's advantage to proceed to trial rather than to multiply the difficulties of his situation by effecting the settlement he did. There is, it must be remembered, no allegation that appellees made any threats of exposing Keane, or that they put him under any duress other than the pressure of their suit.[5] Viewed dispassionately, the settlement bears the earmarks of a compromise be-

[5]There is an allegation that in July 1945—almost a year prior to the settlement—appellees became alarmed at the large sales of Clayton and notified the Clayton Company to stop all further transfers of Clayton shares belonging to Independence, saying that if this were not done they would bring injunction proceedings to prevent further transfers. There is no allegation that this admonition came to Keane's notice or, if so, that it had any effect on his activities, or even that the Clayton Company heeded the notice. We are unable to see the relevancy of the incident as indicating fraud, connivance, or duress on appellees' part.

tween adversaries neither of whom felt entirely confident of his ability to prove his case.

With respect to appellees' knowledge that the settlement of their demands would absorb Clayton shares otherwise claimable by common stockholders it is notable that no facts appear which would place appellees in a trustee relationship toward such stockholders. It is the rule that a stockholder may sue the corporation to recover a dividend declared, since he holds his right to the dividend in his individual capacity. Fletcher, Cyc. Corp., Perm. Ed., Vol. 13, §5922. After the dividend is declared all community of interest in relation to the same as among stockholders themselves and as between them and the corporation is at an end. And the action to recover may be maintained not only by the stockholders recognized by the corporation as entitled to share in the dividend, but by those wrongfully denied the right to share therein. Fletcher, Cyc. Corp., Perm. Ed., Vol. 11, §5365.

The nature of the burden resting on a party who seeks to set aside a judgment for fraud in its procurement is well understood, and counsel are not in serious disagreement as to the applicable principle. The fraud must be extrinsic or extraneous to the issues in the action in which the judgment was rendered. It must have been practiced or connived at by the successful party, and it must be such as prevented the losing party from fully and fairly presenting his case or defense. Zounich v. Anderson, 35 Idaho 792; United

States v. Throckmorton, supra; Toledo Scale Co. v. Computing Scale Co., supra; Donovan v. Miller, supra. Cf. Restatement of the Law of Judgments, §122 (p. 593), Comment "e" (p. 596). Comment "e" of the Restatement is illuminating and we quote it: "Collusion or duress. There is collusion where a party to an action or someone acting on his account induces a fiduciary to neglect or to act contrary to, the interests of the beneficiary. This may be accomplished by a money payment or promise of future benefits to the fiduciary, or by causing him to act out of friendship or by persuasion. Mere knowledge that the fiduciary is neglecting the interests of the beneficiary does not constitute collusion; there must be some cooperation or activity in causing him to act wrongfully."

It must be remembered that a petition to vacate a judgment is addressed to the sound legal discretion of the trial court, and its determination will not be disturbed except for abuse of discretion. Western Union Telegraph Co. v. Dismang, 10 Cir., 106 F. 2d 362, 364; Bush v. Bush, 61 App. D. C. 357, 63, F. 2d 134; In re Rochester Sanitarium & Baths Co., 2 Cir., 222 Fed. 22, 26. Particularly is this true in this instance, where the experienced judge passing on the petition had presided in the litigation in which the judgment was entered, and it is claimed that fraud was practiced upon the court. Certainly we are not able to say that the court's ruling adverse to the petition was wrong.

Affirmed.

DENMAN, Chief Judge, dissenting:

It will be a shock to the legal profession that this court holds, in a proceeding in equity, that stockholders suing á corporation known by them to be entirely controlled by president Keane, also known by them to be a criminal, as yet undisclosed to the public, who has continually robbed the corporation of its Clayton stock[1] and who, as an inducement for their action, threatens them to steal all its remaining Clayton stock,[2] and who was necessarily in fear of exposure by them either by a stockholders' suit for restitution for the thefts or by seeking a criminal prosecution, may secure his stipulation for a judgment against his corporation by which they obtain all the 170,000 Clayton shares the criminal has not yet stolen, a part of which consists of 73,175 shares of Clayton stock which they knew were held in trust by the corporation for other stockholders,[3] without disclosing to the court to which the stipulation is presented and which entered judgment thereon that part of the benefit they received was illegally taken from other stockholders, or the criminal character of the stipulator and what he might fear from those benefited by his action if he could not effect a settlement with them.

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[1]Maj. op., page 5. This, like other facts alleged in the dismissed motion to set aside the judgment, is to be taken as true solely for determining whether a cause of action has been alleged.

[2]Maj. op., page 6.

[3]Maj. op., page 6.

It will also startle the profession that such may be held without mention of, much less consideration of, any of the pertinent cases offered on behalf of appellants, and disposing of their contention on the authority of a text writer, who nowhere states the law to be as stated in the opinion.

The petition's allegations of appellees' connivance with Keane to give them the Clayton shares held in trust for the other stockholders are clear cut. They are:

> ". . . The defendant Company, the Independence Lead Mines Company, now asserts that the said judgment is fraudulent and is a fraud upon this Court and this defendant Company, and makes this motion to set aside the same so this defendant can assert its lawful rights and defend and protect the rights of the holders of the common, assessable stock of this defendant Company; that no disclosure was made to this Court that the award of 170,000 shares of Clayton to the plaintiffs would deprive common assessable stockholders of a dividend previously declared, in the amount of 73,175 shares of Clayton which was a trust for said common stockholders held by the defendant Company and its so-called President, F. C. Keane." (Tr. 70.)
>
> "Upon information and belief, the said defendant alleges the following: That the doings and transactions of the said F. C. Keane in regard to dissipating the cash and funds of the Independence Lead Mines Company and selling the stock of the Clayton Silver Mines Company belonging to the Independence and squandering and dissipating the

> funds realized therefrom for his own benefit, and the extent of the possession by the Independence Lead Mines Company of the sum of only 170,000 shares of Clayton, including over 73,000 shares held in trust for common assessable stockholders, were well known in all particulars to the said plaintiffs long prior to the settlement made in this controversy and the judgment entered therein. . . ." (Tr. 73.)

The law of the state of Independence's incorporation, Arizona, controls with respect to the rights of stockholders against corporate officers who connive with one group of stockholders to give them dividends out of the property to be distributed to other stockholders. National Lock Co. v. Hoagland, 101 F. 2d 575, 582 (Cir. 7). Cf. Harr v. Pioneer Mechanical Corp., 65 F. 2d 332, 334 (Cir. 2).

In the case of Johnson v. Moore, 31 Ariz. 137, 145, there was such connivance by which the corporate officers declared a dividend of the proceeds of the sale of certain company assets and then paid over all the proceeds to certain stockholders to the exclusion of other stockholders. The latter brought suit against both the corporation and the stockholders receiving all the dividend moneys. The Arizona supreme court held, at page 145,

> ". . . If the officers of defendant corporation had merely retained in their custody as such officers plaintiff's share of the proceeds of the sale, his remedy would indeed be *ex contractu*, but the allegation of the complaint is that the corporation

and the individual defendants, with the 'knowledge, consent, aid, and connivance one with the other,' divided among the individual defendants, not only their pro rata of the $42,000 but also that which should have been paid plaintiff. If the trustee of a sum of money pays it to a person not entitled to receive it, with full knowledge on the part of the latter as to the facts, and his active participation in the illegal payment, it is undoubtedly a breach of trust, for which both the trustee and the recipient of the money are liable as in conversion. White v. Sherman, 168 Ill. 589, 61 Am. St. Rep. 132, 48 N. E. 128, Duckett v. National Mech. Bank, 86 Md. 400, 63 Am. St. Rep. 513, 39 L. R. A. 84, 38 Atl. 983; American Trust & Bank Co. v. Boone, 102 Ga. 202, 66 Am. St. Rep. 167, 40 L. R. A. 250, 29 S. E. 182; 38 C. J. 2055. . . ."

Here the claiming owners of 1,000,000 shares take the 75,125 shares belonging to holders of 292,700 by collusion with Keane in control of the corporation. So far as concerns equity, the obligation to return shares thus collusively acquired is no different from where a majority persuades a corporate management to give them all of a dividend to the exclusion of the minority. It is the wrongful control of the corporate officers by which the latter violate a trust for all the stockholders which gives equity its jurisdiction. Hence the following cases of deprivation of a minority of its share of a distribution of corporate assets are applicable. Heinbauch v. Hitchcock, 115 Kan. 182, 222 P. 114; Norse v. Metropolitan S. S. Co., 87 N. J. Eq. 217, 100 A. 219.

The majority opinion does not mention, much less distinguish these cases, offered on behalf of appellants. It cites no authority to the contrary from Arizona or elsewhere. I therefore dissent from its holding "that no facts appear which would place appellees in a trustee relationship toward such stockholders. It is the rule that a stockholder may sue the corporation to recover a dividend declared, since he holds his right to the dividend in his individual capacity. Fletcher, Cyc. Corp., Perm. Ed., Vol. 13, §5922. After the dividend is declared all community of interest in relation to the same as among stockholders themselves and as between them and the corporation is at an end."

Nowhere does Fletcher state that *after* a dividend is declared, one group of stockholders may wrongfully cause the directors to distribute to them the dividends belonging to other stockholders and yet create no trust relationship to those so wronged.

Here is clear Arizona authority that there is community of interest creating a trust relationship between the stockholders where appellees had "knowledge that the settlement of their demands would absorb Clayton shares otherwise claimable by common stockholders."

Independence is still the trustee for the stockholders who have not received their dividend of Clayton shares and owes the duty to recover such specific property (a)

to such stockholders and (b) to the corporation and its creditors[4] to avoid a suit for the value of the shares if the stockholders, denied the distribution of this specific property, sue for its value.

In the discharge of these duties, the present honest officials find a judgment, procured by such connivance, in the road to the recovery of the Clayton shares for the stockholders entitled to them. It is clear that equity requires the removal of the obstruction of that judgment, as here sought.

It seems clear that it was the duty of the appellees to disclose to the court the character of the criminal controlling the corporation and of his proposed settlement depriving the other stockholders of the stock held in trust for them, so offered for their connivance, and have the court appoint for that litigation a trustee for the corporation, who would be free of any such pressure, to defend against the claim of the appellees for his trust res, the Clayton stock.

It is, of course, unfortunate that litigants find themselves required to procure such a substitution, just as it would be unfortunite for them if the person in sole control of the corporation were imbecile or insane.

I dissent from the opinion's statement that to procure such a trustee would require an adjustment of

[4]In this connection the transcript shows at pages 97 and 98 a deficit in earned surplus of $198,597.63 for the year 1943; of $222,948.04 for 1944, and a further net loss of $67,315 for the year 1945.

the internal affairs of the corporation.[5] Even if it required such an adjustment, such a burden would not make the stipulation any the less one procured by the obvious coercive compulsion in the mind of the criminal Keane and one by which the appellees in connivance with him obtain the stock held in trust for other stockholders.

I dissent further from the opinion's statement, seeking to show Keane could have no fear of exposure by appellees, that the holders of the outstanding class A common stock could not sue "effectively" to prevent Keane from further stealing the corporate assets[6] which gave value to the class A common as well as all the other outstanding stock, or to remove Keane as president.

The only ground upon which the maintaining of such a suit could not be "effective" is that their outstanding stock should be cancelled, an issue they had to face in any suit against the corporation and which, if the fact, would defeat their defense to the instant action. Appellees had no such impression of their lack of power to sue effectively when they threatened such a suit to enjoin the Clayton Company to prevent further stealing of Independence's Clayton shares.[7]

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[5]Maj. op., page 5.
[6]Maj. op., page 5.
[7]Maj. op., page 7, footnote.

It is now long established in Arizona, the state of Independence's incorporation, supra, in Idaho, and in the federal courts that stockholders' suits are maintainable in just such a situation of wrongful dealing with the corporate assets, Ryan v. Old Veteran Mining Co., 37 Idaho 625, a stockholders' suit in which the court said, at page 636, "Directors of corporations act in a fiduciary capacity. They hold the corporate property in trust, and any attempt on their part to divert the use of such property to their personal profit or interest is a violation of the trust imposed by virtue of the office. (Riley v. Callahan Mining Co., supra.) [28 Ida. 525.]" Geddis v. Anaconda Mining Co., 254 U. S. 590, 599; Cutting v. Woodward, 255 F. 634 (Cir. 9). This court, by holding or dictum, thus should not overrule or cast doubt upon its own decisions.

I further dissent from the contention of the opinion that the fact that Keane was compelled to disclose his misappropriations nine months after the appellees had wrongfully acquired the 73,175 Clayton shares belonging to other stockholders by virtue of his threat to appellees to steal for himself all the remaining 170,000 shares, warrants the inference that any other stockholder than appellees knew of his thefts when the latter agreed to his stipulation.

There is nothing in the petition inconsistent with its allegation that appellees sought to obtain a better settlement of their claims "by dealing with the so-

called president who desired to conceal the true condition of the affairs of the said Company and his own misdeeds in connection with its operations." That nine months after they made such a settlement he was unable further to conceal his wrongdoing is no evidence that Keane's apprehension of appellees' knowledge of his crimes was not a factor in the negotiation nine months earlier which wrongfully gave to appellees the 73,175 shares belonging to other stockholders.

I further dissent from the opinion's statement that Keane "was *currently* acquiring substantial amounts [plural] of Clayton stock on behalf of Independence." The only statement in this regard is that of the auditor's report (tr. 99) that Keane misappropriated 229,000 shares and that "F. C. Keane reacquired 11,000 shares which were issued as dividends to common stock of the Independence Lead Mines."

This shows a net misappropriation of the 218,000 shares admittedly stolen. Dryden's pearl of a restoration of but 5% of his stealings thus appears to be ersatz. Instead of the purchase being "on behalf of Independence" as stated in the opinion, it is obviously on *behalf of Keane* to restore it to Independence from which, as a part of the dividend already declared, it was distributed before the stipulation was signed and the judgment on it rendered.

That the amount known by appellees to have been stolen when they entered into the stipulation giving

them the 73,175 shares which belonged to the other stockholders is 218,000 shares appears from the following table.

1)	Total Clayton stock held by Independence (Tr. 7)	1,001,000
2)	Amount of Clayton to be distributed (1 Clayton share for each 4 shares of 2,744,700 outstanding common.) (Tr. 67, 68)	686,175
3)	Undistributed Clayton shares remaining (1 minus 2) (Tr. 68)	314,825
4)	Total amount of Clayton sold by Keane and proceeds kept by him (Tr. 99)	229,000
5)	Net amount misappropriated after restoring by Keane of 11,000 shares (Tr. 98, 99)	218,000
6)	Amount of Clayton left in Independence not declared in dividends (2) (3 minus 5)	96,825
7)	Amount of Clayton shares still left in trust of 686,175 dividend (3 above) (Tr. 68, 70)	73,175
8)	Total Clayton remaining in Independence (6 plus 7)	170,000
9)	Amount of Clayton stipulated to be given Kingsbury and Marquardt in settlement (Tr. 69)	170,000
10)	Amount of Clayton left in Independence after settlement (8 minus 9)	0

I dissent also from the opinion's seeking to deprecate the petition by stressing that its allegations concerning the appellees' knowledge of Keane's criminality and their connivance with him to obtain the shares of other stockholders is on information and belief. It is apparent, if the honest successor directors of Independence were not present when the appellees' knowledge was obtained, the wrongful connivance never could have equitable relief, unless they could allege it on information and belief.

The district court erred in holding the petition failed to state a cause of action and its judgment of dismissal should be reversed.

(Endorsed:) Opinion and Dissenting Opinion. Filed Feb. 28, 1949. Paul P. O'Brien, Clerk.

Opinion and Dissent of Court of Appeals Dated August 8, 1949

In the United States Court of Appeals for the Ninth Circuit

INDEPENDENCE LEAD MINES COMPANY, a corporation, *Appellant*,

vs.

ALMA R. KINGSBURY AND OLGA MARQUARDT, *Appellees*.

No. 11,959

Order Denying Petition for Rehearing in Banc

Before: DENMAN, Chief Judge, and HEALY and ORR, Circuit Judges.

The petition for rehearing in banc is denied.

DENMAN, Chief Judge, dissenting: This appeal is clearly one requiring a rehearing in banc, for the reasons stated in my dissent filed on February 28, 1949, and the further reasons here stated.

The court's opinion establishes for this circuit as proper conduct for an attorney, an officer of the federal courts, here of two widowed women clients, an unethical wrong which stands out like the sore thumb of colloquial speech. By such unethical wrong was

prevented a decision of the merits affecting stockholders not joined as parties, for whom Independence was trustee.

The issue presented by the complaint, upon which the challenged judgment rests, is whether the appellees' stock in Independence entitled them to participate with other Independence stockholders, not joined in the action, in the distribution of the Clayton shares declared as a dividend solely to other stockholders. Some of these other stockholders had received their dividend, others had not. None was joined in the action.

The motion charges that appellee widows and hence appellees' attorney knew that Independence's president Keane, the sole manager of the defendant, had embezzled so many of the Clayton shares that there were not enough left to make a full distribution to the stock of appellees and the other absent stockholders, if the court decided appellees' stock entitled to participate in the dividend.

With such knowledge it at once became the duty of the attorney for appellees, plaintiffs in the case, to advise the court that Independence, with Keane its sole manager, could not act as trustee for the absent other stockholders in the litigation which, if successful, so affected their right to the insufficient remaining unembezzled shares. The attorney should have asked

the court either to substitute some unprejudiced person in Keane's place or for a joinder of the absent stockholders so known by appellees to have been wronged by Keane.

That Keane realized this is apparent from the desperate means he took to avoid such a disclosure of his crimes. He had one Sekulic advise appellees that if they did not enter into a stipulation by which they received *all* the unembezzled shares of Clayton, *he would proceed to embezzle all the remaining shares.*

In this situation it became the duty of appellees' attorney to advise the court at once and procure an injunction against Keane, to protect not only Independence from such threatened last embezzlement of its Clayton shares but also to protect the other stockholders and his own clients.

Instead, the bait of acquiring all the remaining Clayton shares to the exclusion of the other shareholders was too alluring, and Keane's stipulation was signed by appellees' attorney and presented to the court. By this conduct he secured for his clients the judgment so depriving the absent stockholders of their day in court as to the conflicting claims of the appellees, and depriving them of the Clayton shares to some part of which they were entitled even if appellees established their claim to participate in the Clayton dividend.

It has been suggested that the stipulation by which the appellees acquired the Clayton stock belonging to the unjoined Independence shareholders may be valid because supported by a consideration to Independence consisting of the surrender by appellees of a part of appellees' Independence shares.

This suggestion is clearly untenable. The motion to set aside the judgment alleges that the issue of the shares held by appellees was fraudulently procured by appellees' husbands, from whom they acquired their present interest by inheritance. See paragraphs III, IV and V of motion, transcript pages 54, 58. The surrender of such fraudulently procured shares is no consideration to the company from which they were taken.

Attention is again called to the fact that the cases cited on behalf of appellant, showing the Idaho law controlling in this suit, declaring the trust relationship of a corporation to its shareholders with regard to dividends declared and not distributed, *are not only not considered and distinguished, if possible, but also not even mentioned.*

Such ignoring of cogent and pertinent contentions seems also to raise a question with respect to the obligation of an appellate court to its litigants.

(Endorsed:) Order on Petition for Rehearing and Dissenting Opinion of Denman, C. J. Filed Aug. 8, 1949. Paul P. O'Brien, Clerk.

Amended Order of Court of Appeals Dated August 22, 1949

In the United States Court of Appeals for the Ninth Circuit

INDEPENDENCE LEAD MINES COMPANY, a corporation, *Appellant*, vs. ALMA R. KINGSBURY AND OLGA MARQUARDT, *Appellees.*	No. 11,959 Order

The order of the Court entered August 8, 1949, is amended as follows: The words "Order Denying Petition for Rehearing in Banc" are stricken, and the order itself is amended to read as follows: "The petition for rehearing is denied."

Dated August 22, 1949.

WILLIAM HEALY,
United States Circuit Judge.

WM. E. ORR,
United States Circuit Judge

(Endorsed)
Filed: August 22, 1949.
PAUL P. O'BRIEN, *Clerk.*

Amended Dissent of Chief Judge Denman Dated August 23, 1949

In the United States Court of Appeals for the Ninth Circuit

INDEPENDENCE LEAD MINES COMPANY, AN ARIZONA CORPORATION, *Appellant,*

vs.

ALMA R. KINGSBURY AND OLGA MARQUARDT, *Appellees.*

No. 11959

Order

IT IS ORDERED that my dissenting opinion filed herein on August 8, 1949, be amended by inserting therein, after its first paragraph, the following:

(A) *The attempt of two judges in a panel of three judges to deny a petition for rehearing in banc violates the law as established in United States v. Johnston,* 316 *U. S.* 649, 650, *and Textile Mills Corp. v. Commissioner,* 314 *U. S.* 326, 333, *et. seq.*

The order of August 22, 1949, of this panel of this court does not truly describe its action. What it attempts to do is to deny a petition to the court in banc for a rehearing by our whole court of seven judges. The amendment of August 22, 1949, attempts to conceal the fact disclosed in the order as first entered on August 8, 1949. The August 8th order is entitled,

"Order denying petition for rehearing in banc," and the order of that date reads, "The petition for rehearing en banc is denied."

In this, the first order followed the wording of the petition to the court in banc reading, "Petition for rehearing en banc," which prayed, "Appellant respectfully prays that this cause be reheard and considered in banc and prays for a reconsideration of the opinion filed herein of February 28, 1949, by reason of the dissenting opinion likewise filed herein and because of the following points . . ."

In view of the Supreme Court decisions cited above, it is too obvious to need argument that two judges cannot thus assume to act on a petition addressed to seven judges.

(B) *Further grounds of dissent.*

WILLIAM DENMAN,
Chief Judge United States Court of Appeals, Ninth Circuit.

(Endorsed)
Filed: August 23, 1949.
PAUL P. O'BRIEN, *Clerk.*